

ST 03-14

Tax Type: Sales Tax

Issue: Responsible Corporate Officer – Failure to File or Pay Tax

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS**

THE DEPARTMENT OF REVENUE)	Docket No.	02-ST-0000
OF THE STATE OF ILLINOIS)	IBT No.	0000-0000
v.)	NPL No.	0000
JOHN DOE , as responsible)		
officer of ABC, Inc.,)	John E. White,	
Taxpayer.)	Administrative Law Judge	

RECOMMENDATION FOR DISPOSITION

Appearances: Mr. Gerald Gold, Karaganis & Gold, appeared for John Doe; Mr. Michael Abramovic, Special Assistant Attorney General, appeared for the Illinois Department of Revenue.

Synopsis:

This matter arose when John Doe (“taxpayer” or “Doe”) protested a Notice of Penalty Liability the Illinois Department of Revenue (“Department”) issued to him as a responsible officer of ABC, Inc. (“ABC”). Notice of Penalty Liability (“NPL”) number 0000 assessed a penalty equal to the unpaid Retailers’ Occupation Tax (“ROT”) liability of the corporation from sales made during the months of January 1996 through and including December 31, 1999. The penalty was a personal liability penalty, pursuant to § 3-7 of Illinois’ Uniform Penalty and Interest Act (“UPIA”).

A hearing was held at the Department’s offices in Chicago. At hearing, taxpayer introduced evidence consisting of, *inter alia*, ABC’s books and records, the testimony of one of ABC’s former outside accountants, and his own testimony. I have reviewed the evidence adduced at hearing, and I am including in this recommendation findings of fact and conclusions of law. I recommend that the penalty be assessed against taxpayer.

Findings of Fact:

Facts Regarding ABC's Organization and Operations

1. ABC is a corporation that conducted business in Illinois as a distributor of laboratory equipment. Department Group Ex. 1, p. 7 (auditor's comments).
2. ABC was incorporated in Illinois in 1987. Stipulation ("Stip.") Ex. 3, pp. 13-15 (copies of, respectively, Articles and Certificate of Incorporation). It was wholly owned by XYZ Corporation. *Id.*, p. 17 (Action by the Shareholder of ABC, Inc.).
3. At its inception, Doe owned 50.5% of XYZ Corp. Hearing Transcript ("Tr."), p. 43 (testimony of Doe). In 1996, Doe become 100% owner of XYZ Corp. Stip. Group Ex. 3, pp. 74-76 (written consent resolutions of the shareholders and directors of ABC, Inc.); Tr. p. 57 (Doe).
4. ABC ceased doing business in Illinois on or about March 2000, and a NUC-10, discontinuation of business form, was prepared to document that discontinuation. Department Group Ex. 1, p. 9 (auditor's comments).
5. ABC filed monthly returns for the months during 1996. Department Group Ex. 1, p. 7 (auditor's comments). It was required to file quarterly returns for 1997 and 1998, and was required to file an annual return regarding 1999. *Id.*
6. ABC did not file returns for the last three quarters of 1998, and it did not file its 1999 annual return. Department Group Ex. 1, p. 7 (auditor's comments).
7. The Department conducted an audit of ABC for the period beginning on January 1, 1996 through and including December 31, 1999. Department Group Ex. 1, pp. 2-3 (copies of, respectively, the Notice of Assessment issued to ABC, and the audit report prepared by the Department's auditor upon the completion of the

audit).

8. Shortly after the audit began, Doe became the Department's contact with ABC. Department Group Ex. 1, pp. 10-20 (audit history worksheet).
9. Following audit, the Department auditor prepared a return showing that ABC owed tax in the amount of \$21,640.00, and a late filing penalty in the amount of \$258. Department Group Ex. 1, p. 3.
10. The auditor notified Doe of his determinations via certified mail on or about October 25, 2000. Department Group Ex. 1, pp. 8 (auditor's comments), 19 (audit history worksheet).
11. The audit was completed in December, 2000, and Doe signed the auditor-prepared audit return on December 11, 2000. Department Group Ex. 1, pp. 3 (copy of auditor-prepared return), 8 (auditor's comments), 20 (audit history worksheet).
12. At the time the audit was completed, Doe told the auditor that ABC could not pay the tax, because the corporation's assets were in the hands of its creditors. Department Group Ex. 1, pp. 8-9 (auditor's comments), 20 (audit history worksheet). No documentary evidence, however, corroborated that such a transfer of ABC's assets to its creditors, in fact, occurred, or when such a purported transfer might have occurred.
13. After ABC did not pay the liability determined by audit within thirty days of the date Doe signed the auditor-prepared return, a late payment penalty was assessed. Department Group Ex. 1, p. 2 (Notice of Assessment).
14. Throughout the period at issue, Doe was ABC's president, secretary and director.

- Department Group Ex. 1, pp. 39-42 (copies of ABC's annual reports to the Illinois Secretary of State for 1996 – 1999).
15. From 1997 through 1999, Doe was ABC's sole officer and director. *Id.*, pp. 39, 41-42.
 16. Doe had the authority to sign and issue checks drawn on ABC's accounts to pay corporate and other debts. Stip. Ex. 4 (stipulation of the parties), ¶ 4.
 17. ABC's controllers did not have check-signing authority. Tr. pp. 51-52 (Doe).
 18. During discovery in this matter, Doe produced approximately 3,000 checks drawn on ABC's accounts during the audit period. Stip. Ex. 4, ¶ 4. The parties agreed that Doe signed approximately 5% of those checks. Stip. Ex. 4, ¶ 4.
 19. One check Doe signed was drawn to the order of the Pennsylvania Department of Revenue, Bureau of Receipts, in the amount of \$3,117.67. Stip. Group Ex. 2, (check no. 5781). The check was drawn to pay a first quarter 1997 tax liability. *Id.* Doe's signature is the only signature on the face of the check. *Id.*
 20. Another check Doe signed, on the same day, was drawn to the order of the New Jersey Sales Tax, and it too was drawn to pay a first quarter 1997 tax liability. Stip. Group Ex. 2 (check no. 5782). Doe's signature is the only signature on the face of the check. *Id.*
 21. Other ABC checks drawn and signed by Doe were paid to Doe's order (Stip. Group Ex. 1 (check nos. 8294, 8299, 8303, 8314, 8315, 8320, 8326)), and to the order of Jane Doe. Stip. Group Ex. 1 (check nos. 8293, 8296, 8297, 8300, 8305, 8307, 8312, 8313, 8321, 8324, 8325, 8350). All of these checks were presented for payment and paid. Stip. Group Ex. 1 (check nos. 8294, 8299, 8303, 8314,

8315, 8320, 8326 (Doe), 8293, 8296, 8297, 8300, 8305, 8307, 8312, 8313, 8321, 8324, 8325, 8350 (Jane)).

22. Some of the checks Doe signed that were made payable to himself or to Jane Doe were drawn during periods regarding which ABC had not filed sales and use tax returns. Stip. Group Ex. 1 (check nos. 8314, 8315, 8320, 8326 (Doe), 8312, 8313, 8321, 8324, 8325, 8350) (Jane)).
23. After February 12, 1998, Doe's signature was the only signature on the checks included within Stip. Group Ex. 1. Stip. Group Ex. 1.

Conclusions of Law:

When the Department introduced the NPL into evidence under the certificate of the Director, it presented *prima facie* proof that Doe was personally responsible for ABC's unpaid tax liabilities. 35 ILCS 735/3-7; Branson v. Department of Revenue, 68 Ill. 2d 247, 260, 659 N.E.2d 961, 968 (1995) ("by operation of the statute, proof of the correctness of such penalty, including the willfulness element, is established by the Department's penalty assessment and certified record relating thereto."). The Department's *prima facie* case is a rebuttable presumption. Branson, 168 Ill. 2d at 262, 659 N.E.2d at 968. After the Department introduces its *prima facie* case, the burden shifts to the taxpayer to establish that one or more of the elements of the penalty are lacking. *Id.*

Section 3-7 of the UPIA provides that a personal liability penalty liability may be imposed upon:

- (1) Any officer or employee of any corporation ... who has the control, supervision or responsibility of filing returns and making payment of ... the tax[es] ... imposed ... **and** who willfully:

- (2) fails to file such return **or**
- (3) [fails] to make such payments to the Department **or**
- (4) ... attempts ... in any other manner to evade or defeat the tax

35 ILCS 735/3-7 (emphasis added).

Taxpayer contends that while he was an officer of ABC, he was not an officer who was responsible for preparing and filing the corporation's sales tax returns, or who was responsible for paying its sales tax liabilities. [Taxpayer's] Closing Argument and Brief in Support ("Taxpayer's Brief"), p. 3. Specifically, Doe argues:

... The Department's exhibits reflect that the NUC-1 when ABC, began doing business in Illinois, was executed by the controller as the responsible person, not Doe who signed as president. Doe had no participation in the preparation, filing or paying of Federal payroll, unemployment or "sales" tax returns in any of the states ABC operated in. Doe had no participation or decision in the decisions as to what creditors of ABC were paid or not. Doe also had no knowledge whatsoever that any taxes were due the Department. ***

Taxpayer's Brief, p. 3.

Doe's contentions, however, are not supported by the text of UPIA § 3-7 or by the documents in the record. First, the fact that Doe did not sign the NUC-1 as the person who undertook individual responsibility for filing the corporation's sales and use tax returns, and for paying the corporation's retailers' occupation taxes, does not foreclose a conclusion that Doe was a responsible officer of ABC. More than one individual can be a responsible officer or employee of a corporation. 35 ILCS 735-3-7 (personal liability may be imposed on "any [responsible] officer or employee ...") (emphasis added); *see also, e.g., Estate of Young v. Department of Revenue*, 316 Ill. App. 3d 366, 734 N.E.2d 945 (1st Dist. 2000) (affirming determination that two brothers, respectively, the

corporation's president and vice-president, were personally liable for the corporation's unpaid ROT liabilities). Thus, an individual who signs as the responsible person on a NUC-1 form does not agree to undertake sole, or exclusive, responsibility for the corporation's tax liabilities. *See* Department Group Ex. 1, p. 36 (copy of page 2 of ABC's prepared NUC-1). Nor does the NUC-1 form, itself, purport to fix the determination of those who may be subject to personal liability under § 3-7 solely to the individual who signs as the responsible person. *See id.*

The record here, moreover, discloses that ABC had different controllers during the audit period. Tr. pp. 101-110 (Doe). Doe hired Smith (Tr. p. 101-102 (Doe)), and Doe was the only ABC officer and director who could have hired its subsequent controllers after Smith left. Stip. Group Ex. 3, pp. 39, 41-42. As described below, Doe had the authority and responsibility to supervise ABC's controllers' activities, at least as those activities involved filing ABC's Illinois ROT returns, and paying its ROT liabilities.

Doe testified, and he argued following hearing, that he had no knowledge whatsoever that any taxes were due the Department. Tr. pp. 54-60 (Doe); Taxpayer's Brief, p. 3. But that testimony is inconsistent with the statements Doe ratified when he signed the NUC-1 ABC completed when it sought to do business in Illinois. On page 2 of that form, ABC stated that it would be selling merchandise at retail from Illinois. Department Group Ex. 1, p. 36. On the same page, ABC stated that it would have a monthly ROT and/or use tax liability of approximately \$200.00. Doe signed page 4 of that form, under the following statement, "Under penalties of perjury, I state that I have examined this application and it is true and correct." *Id.*, p. 38. Doe, therefore, knew —

at a minimum — that ABC might have an ongoing Illinois ROT liability so long as it was engaged in the business of retailing in Illinois. Indeed, he knew that ABC would have an estimated ongoing monthly liability of about \$200.00.

Most importantly, Doe was, during most of the audit period, ABC's sole officer and director, and a person in that position cannot credibly plead ignorance regarding the corporation's duties to file returns and pay taxes — especially once he has already acknowledged those obligations in writing. *See Branson v. Department of Revenue*, 68 Ill. 2d 247, 267, 659 N.E.2d 961, 971 (1995) (“... we do not intend to imply that a corporate officer who is responsible for filing retailers’ occupation tax returns and remitting the collected taxes may avoid personal liability ... merely by delegating bookkeeping duties to third parties and failing to inspect corporate records or otherwise failing to keep informed of the status of the retailers’ occupation tax returns and payments.”). After he signed ABC's NUC-1, the only way for Doe credibly to maintain that he did not know that ABC had an Illinois ROT liability would be if he personally reviewed ABC's sales activities for the appropriate period and determined that none of the sales were subject to Illinois ROT. There is no such evidence in this record. And regardless of ABC's actual periodic liability, Doe must be deemed to know that ABC would always have an Illinois ROT *reporting* obligation, so long as it was engaged in the business of retailing in Illinois. Department Group Ex. 1, p. 38.

Doe's argument that he had no participation in the preparing, filing or paying ABC's federal, payroll, unemployment or sales tax returns in any of the states in which ABC operated, is similarly contradicted by the record. Initially, Doe was asked the following questions and gave the following answers on direct examination:

Q: Who would supervise and prepare the state sales tax returns?

A: Controller.

Q: Did you ever prepare them?

A: No.

Q: Did you ever sign them?

A: I might have if he told me to sign one if I was around at the time.

Tr. p. 55 (Doe). Thus, Doe admits at least the possibility that he signed ABC's Illinois ROT returns, which admission is, itself, inconsistent with an argument that he had absolutely nothing to do with such activities.

More direct evidence of Doe's authority and responsibility for filing ABC's state tax returns, and paying its state tax liabilities, is found within the documentary evidence of record. Among the checks that Doe drew to pay ABC's liabilities were two that he drew to pay ABC's tax liabilities for the first quarter 1997 in New Jersey and in Pennsylvania. Stip. Group Ex. 2 (check nos. 5781 & 5782). Doe was the only individual who signed the face of those two checks. *Id.* Moreover, Doe testified that none of ABC's different controllers had check-writing authority. Tr. pp. 51-52 (Doe). That means that someone other than the controller had to sign whatever checks were prepared to pay any of ABC's tax liabilities, including its Illinois ROT liabilities. At best, the evidence in this case establishes that Doe may not have been the individual who ordinarily signed checks drawn to pay ABC's tax liabilities. *Compare id. with* Tr. p. 53 (Doe). But there is no credible documentary evidence to show that he lacked any responsibility, control or supervision over ABC's payment of such taxes. Clearly, he had such authority, and he exercised it. Stip. Group Ex. 2 (check nos. 5781 & 5782).

Additionally, a corporate officer is required to sign a corporation's Illinois ROT returns to make sure that someone with actual personal knowledge of the corporation's

activities review the return and then attest, under penalty of perjury, that the information included on the return is true and correct. 86 Ill. Admin. Code § 130.525(a) (“Returns must be signed by the president, vice president, secretary or treasurer, or by the properly accredited agent whose power of attorney is on file with the Department, if the seller is a corporation.”). Doe’s testimony that the controllers of ABC prepared and filed ABC’s returns does not change that requirement. Tr. pp. 55-56 (Doe). As this case shows, a person employed by a corporation as its controller need not be a corporate officer, and ABC’s controllers could well have signed the corporation’s returns as the preparer. At a minimum, Doe failed to offer any evidence that ABC’s controllers signed returns as ABC’s agents, under power of attorney. Without proof that ABC had given power of attorney to someone other than its sole officer to sign its returns, as the taxpayer, Doe was the only person authorized — and required — to sign them, as the taxpayer. 86 Ill. Admin. Code § 130.525(a); Stip. Group Ex. 3, pp. 39, 41-42 (ABC’s annual returns with the Illinois secretary of state, showing that Doe was ABC’s sole officer and director in 1997-1999).

Further, the fact that Doe signed 5% of the ABC checks drawn during the audit period contradicts Doe’s argument that he had no part in any decision regarding which of ABC’s creditors were paid. When a person signs and issues a check, that person has purposefully acted to ensure that a certain amount of funds will be paid to a specific person. *See* 810 ILCS 5/3-104(a), (f). I do not believe that Doe signed ABC checks accidentally. Rather, I conclude that Doe signed those ABC checks because, in each case, he made a conscious decision that the named payee should be paid a sum certain in money. It is further reasonable to conclude that each of the payees named on the checks

Doe signed was a ABC creditor, or someone to whom ABC was obliged to pay some amount of money. Contrary to Doe's testimony at hearing, every time he signed a ABC check, or approved an account payable, he made a decision regarding which of ABC's creditors would be paid, or how its corporate funds would be expended.

That 95% of ABC's checks were signed by individuals other than Doe, moreover, does not prove, as taxpayer suggests, that others had responsibility over ABC's finances that Doe lacked. *See* Taxpayer's Brief, p. 4. It is more reasonable to conclude that Doe — ABC's sole owner, officer and director — delegated to those other individuals the authority to sign ABC checks. As the Illinois Supreme Court has indicated, delegation of duties to others does not make an otherwise responsible officer immune from personal liability over the corporation's unpaid tax liabilities. Branson, 68 Ill. 2d at 267, 659 N.E.2d at 971. Doe's burden is to show that he lacked the control, supervision or responsibility for filing ABC's tax returns and paying ABC's taxes. *Id.*, at 260, 659 N.E.2d at 968; 35 ILCS 735/3-7. In some instances, perhaps, establishing that one signed only a fraction of a corporation's checks might help satisfy that burden. Here, however, even though Doe signed only a small fraction of ABC's checks, among the checks he *did* sign were two for ABC's state tax liabilities. Stip. Group Ex. 2 (check nos. 5781 & 5782). Because of his status within the corporation, moreover, Doe was also required by law to sign ABC's Illinois ROT returns. 86 Ill. Admin. Code § 130.525(a). Doe, therefore, did not carry his burden to show that the Department erred in deciding he was subject to a § 3-7 penalty.

Doe also personally drew and signed ABC checks to pay himself and Jane Doe during periods regarding which ABC did not file returns to report and to pay its Illinois

ROT liabilities. *Compare* Stip. Group Ex. 1 (check nos. 8314, 8315, 8320, 8326 (Doe), 8312, 8313, 8321, 8324, 8325, 8350) (Jane)) with Department Group Ex. 1, p. 7 (identifying the last three quarters of 1998, and the year of 1999, as “open periods,” meaning periods for which no returns were filed). ABC failed to file returns for the last three quarters of 1998, and it failed to file an annual return for 1999. Department Group Ex. 1, p. 7. During that time, when ABC was making sales subject to Illinois ROT, and not filing returns to report and to pay its Illinois ROT liabilities pursuant thereto, Doe was personally drawing and signing ABC checks to pay corporate funds to himself and to others. Stip. Group Ex. 1 (check nos. 8314, 8315, 8320, 8326 (Doe), 8312, 8313, 8321, 8324, 8325, 8350) (Jane)).

Finally, Doe argues that the testimony of ABC’s independent accountant shows that ABC’s controllers, and not Doe, were the individuals who were responsible for all things financial at ABC. Specifically, taxpayer argues that:

... Doe’s testimony and the Department’s stipulation [that Doe signed 5% of the checks and account payable approvals reviewed during discovery] were further supported by an independent Certified Public Accountant who reviewed ABC’s yearly records and financials. His testimony clearly reflect that in dealing with payables, tax liabilities, and preparation of Federal income tax returns, he dealt solely with the controller and his department and the employees under his control. At no time was Doe consulted as Doe had no knowledge of the financial day to day company operations. Additionally, the independent auditor was totally unaware of any liabilities due the Department during his tenure by ABC.

Taxpayer’s Brief, p. 4.

Doe is correct that Jones testified that the overwhelming majority of his contacts with ABC were with its controllers (Tr. pp. 141-143 (testimony of Mr. Jones (“Jones”))),

and that, when he left the firm for whom he reviewed ABC's business, he never had any knowledge that ABC had Illinois sales tax liabilities. Tr. p. 148 (Jones). But Jones further testified that he never prepared any of ABC's Illinois sales tax returns (Tr. p. 141), that he did not audit ABC's books and records (Tr. p. 150), and that he had no recollection of whether ABC had business activities in Illinois that required it to pay Illinois sales tax. Tr. p. 151 (Jones). Jones had less personal knowledge of ABC's business activities than Doe did. None of his testimony, moreover, detracts from the evidence in this record showing that Doe, ABC's sole officer and director, was a person with the control, supervision or responsibility for filing ABC's returns and paying its Illinois taxes.

Conclusion:

I recommend that NPL No. 0000 be finalized as issued, with interest to accrue pursuant to statute.

Date: 9/16/2003

John E. White
Administrative Law Judge